

OPEN MEETING ITEM



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COMMISSIONERS
MIKE GLEASON - Chairman
WILLIAM A. MUNDELL
JEFF HATCH-MILLER
KRISTIN K. MAYES
GARY PIERCE

ORIGINAL



ARIZONA CORPORATION COMMISSION

22

DATE: NOVEMBER 29, 2007

DOCKET NO: E-01575A-07-0501

TO ALL PARTIES:

Enclosed please find the recommendation of Administrative Law Judge Jane Rodda. The recommendation has been filed in the form of an Opinion and Order on:

SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC.
(FINANCING)

Pursuant to A.A.C. R14-3-110(B), you may file exceptions to the recommendation of the Administrative Law Judge by filing an original and ten (10) copies of the exceptions with the Commission's Docket Control at the address listed below by 4:00 p.m. on or before:

DECEMBER 10, 2007

The enclosed is NOT an order of the Commission, but a recommendation of the Administrative Law Judge to the Commissioners. Consideration of this matter has tentatively been scheduled for the Commission's Working Session and Open Meeting to be held on:

DECEMBER 17 and DECEMBER 18, 2007

For more information, you may contact Docket Control at (602) 542-3477 or the Hearing Division at (602) 542-4250. For information about the Open Meeting, contact the Executive Secretary's Office at (602) 542-3931.

Arizona Corporation Commission
DOCKETED

NOV 29 2007

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BRIAN C. McNEIL
EXECUTIVE DIRECTOR

AZ CORP COMMISSION
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1 **BEFORE THE ARIZONA CORPORATION COMMISSION**

2 **COMMISSIONERS**

3 MIKE GLEASON - Chairman
4 WILLIAM A. MUNDELL
5 JEFF HATCH-MILLER
6 KRISTIN K. MAYES
7 GARY PIERCE

8 IN THE MATTER OF THE APPLICATION OF
9 SULPHUR SPRINGS VALLEY ELECTRIC
10 COOPERATIVE, INC. FOR AUTHORIZATION
11 TO INCUR DEBT TO FINANCE ITS CLEAN
12 RENEWABLE ENERGY BONDS FOR SCHOOLS
13 PROGRAM AND FOR RELATED APPROVALS.

DOCKET NO. E-01575A-07-0501

DECISION NO. _____

14 **OPINION AND ORDER**

11 Open Meeting
12 December 18 and 19, 2007
13 Phoenix, Arizona

14 **BY THE COMMISSION:**

15 * * * * *

16 Having considered the entire record herein and being fully advised in the premises, the
17 Arizona Corporation Commission ("Commission") finds, concludes, and orders that:

18 **FINDINGS OF FACT**

19 1. On July 27, 2007, Sulphur Springs Valley Electric Cooperative, Inc. ("SSVEC" or
20 "Cooperative"), an Arizona class "A" public service corporation and non-profit cooperative, filed an
21 application with the Commission for authorization to incur debt to finance its Clean Renewable
22 Energy Bonds for Schools Program ("CREBS Program") and for related approvals.

23 2. On September 27, 2007, SSVEC filed an affidavit of publication verifying that it had
24 published the public notice of its financing application in the *Eastern Arizona Courier* on September
25 9, 2007, in the *Sierra Vista Herald/Bisbee Daily Review* on September 11, 2007, and in the *San*
26 *Pedro Valley News-Sun* and the *Arizona Range News* on September 12, 2007.

27 3. On November 16, 2007, the Commission's Utilities Division Staff ("Staff") filed its
28 Staff Report, recommending approval of the application.

1 4. On November 19, 2007, SSVEC filed a Response to the Staff Report. SSVEC had no
2 comments on the substance of the Staff recommendations, but requested that the Commission
3 consider the application at its regularly scheduled December Open Meeting so that the matter could
4 be approved before the end of the year. The Cooperative states that the contractor's bid to install the
5 photovoltaic shade structures at all public schools in SSVEC's service territory will expire at the end
6 of the year and failure to approve the project by then will require a re-bid of the project and result in
7 higher costs to SSVEC primarily as a result of recent increases in the price of steel. SSVEC states
8 further that because of the inter-relationship between the two dockets, the Commission should
9 consider approval of the Renewable Energy Standard Tariff ("REST Plan" or "RES Tariff") at the
10 same time as the current financing request.

11 5. SSVEC is an Arizona non-profit, member-owned cooperative that provides electric
12 distribution service to approximately 49,000 customers in parts of Cochise, Santa Cruz, Pima and
13 Graham Counties. The Cooperative's headquarters is in Willcox, Arizona.

14 6. The Commission approved SSVEC's current rates in Decision No. 58358 (July 23,
15 1993).

16 7. SSVEC is seeking Commission authorization to obtain debt financing through an
17 \$11.48 million credit facility from the National Rural Utilities Cooperative Finance Corporation
18 ("CFC"). SSVEC also requests authorization from the Commission to pledge, mortgage, lien and/or
19 encumber its assets in connection with the CFC credit facility.

20 8. The purpose of the financing is to construct photovoltaic ("PV") shade structures at all
21 the public schools in SSVEC's service territory as well as at public colleges and universities. This
22 program is a major part of SSVEC's REST Plan that is currently before the Commission for approval
23 in Docket No. E-01575A-07-0310. In its Response to the Staff Report SSVEC states that the source
24 of revenue for payment of the CREBS Program loan will come directly from SSVEC's proposed
25 REST Tariff which has been incorporated into the REST Plan.

26 9. The CREBS Program is expected to lower the energy bills of 41 schools. The
27 Program will install a total of 41 systems, each system will produce 23 KW of electricity at peak
28 output. SSVEC will not charge the schools for the electricity produced by the PV systems. The

1 CREBS Program will provide an educational opportunity for the schools, via a cable connection to a
2 computer in the school library which will show students and faculty how the system is working.
3 SSVEC prepared an economic analysis of the school PV systems; depending upon system outputs
4 and annual energy cost increases, SSVEC's cost recovery analysis estimates that the cost recovery, or
5 payback, for the school PV systems will range from 16.7 to 27.8 years.¹

6 10. SSVEC received CFC approval for the Credit Facility on July 6, 2007. The
7 Cooperative estimates an interest rate on the loan of approximately 0.5 percent with a maximum term
8 of 16 years. The CFC loan will be subject to a fee of 150 basis points to cover the legal expenses,
9 placement fees and administrative costs. Under the CFC commitment, the funds may be used for
10 reimbursement of qualified CREBS Program project expenses only.

11 11. The Commission's Engineering Staff has reviewed the SSVEC CREBS Program and
12 Financing Application and finds that the Program is appropriate to meet a portion of SSVEC's
13 Renewable Energy Standard and Tariff requirements.

14 12. Staff agrees with SSVEC that the CREBS PV program will benefit all of SSVEC's
15 customers who will provide funding through the RES Tariff. SSVEC's customers are the same
16 parties who provide funding for the local schools by means of local taxes. Staff believes that the
17 school PV program was the result of customer focus groups that clearly showed SSVEC customer
18 support for such a program.

19 13. Staff finds the costs of the CREBS Program to be reasonable.

20 14. Staff cautions that its conclusions should not be interpreted to imply a specific
21 treatment for rate base or rate-making purposes in the Cooperative's future rate filings.

22 15. Staff performed a financial analysis of the effect of the proposed debt. As of year end
23 December 31, 2006, the Cooperative had a capital structure consisting of 3.4 percent short-term debt,
24 62.4 percent long-term debt and 34.2 percent equity. As of December 31, 2006, the Cooperative had

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28 ¹ Under SSVEC's analysis, if annual energy costs increase at a 4 percent rate each year, the SSVEC calculations estimate a 17.8 year payback for a perfect system performance and a 19 year payback if the performance is 80 percent of the perfect peak output. The longest payback calculated by SSVEC is 27.8 years, and assumes annual energy costs do not increase at all. Staff's analysis suggests a payback in the range of 28-30 years based on more conservative assumptions.

1 a Times interest Earned Ratio ("TIER") of 1.80 and Debt Service Coverage Ratio ("DSC") of 1.56.²
 2 Based on year end 2006 data, the addition of \$6.8 million in previously authorized debt, and the
 3 proposed new debt of \$11.48 million associated with the CREBS Program, the Cooperative's capital
 4 structure would consist of 3.5 percent short-term debt, 66.6 percent long-term debt and 29.9 percent
 5 equity, and its TIER would drop to 1.61 and its DSC to 1.49. In Docket No. E-01575A-07-0446,
 6 SSVEC requested authority to borrow \$70.43 million from the CFC to fund its 2008-2009
 7 Construction Work Plan ("CWP"). Staff performed a pro forma analysis that assumed a \$35.03
 8 million draw related to the CWP, and based on a term of 35 years and an interest rate of 7.5 percent,
 9 determined that based on December 2006 numbers, the Cooperative's projected 2008 capital structure
 10 would consist of 2.94 percent short-term debt, 72.92 long-term debt and 24.14 percent equity; and
 11 would have a TIER of 1.26 and DSC of 1.37. Staff's projections indicate that with an additional \$35
 12 million draw related to the CWP, in 2009, all else remaining equal, the Cooperative would have a
 13 capital structure consisting of 2.6 percent short-term debt, 77.1 percent long-term debt and 20.3
 14 percent equity, a TIER of 0.76 and DSC of 1.06.³

15 16. Staff notes that its pro forma TIER indicates that operating income would become
 16 insufficient to cover interest expense in 2009, and would be unsustainable in the long-run. Staff states
 17 that the DSC indicates that SSVEC will be able to meet all debt obligations with cash generated from
 18 operations. Staff notes further that should the Commission approve the proposed RES Tariff, SSVEC
 19 would have incremental revenue to service the loan and have a higher DSC, all else being equal.⁴

20 17. Staff states further that it typically recommends cooperatives have a minimum equity
 21 ratio of 30 percent as being appropriate to balance the cost of debt and financial risk. Staff

22 ² TIER represents the number of times earnings cover interest expense on short-term and long-term debt. A TIER greater
 23 than 1.0 means that operating income is greater than interest expense. A TIER less than 1.0 is not sustainable in the long
 term but does not mean that debt obligations cannot be met in the short run.

24 DSC represents the number of times internally generated cash will cover required principal and interest payments on
 25 short-term and long-term debt. A DSC greater than 1.0 indicates that operating cash flow is sufficient to cover debt
 26 obligations. A DSC less than 1.0 means that debt service obligations cannot be met by cash generated from operations
 and that another source of funds is needed to avoid default.

27 ³ Staff's pro forma analysis reflects the Cooperative's projected figures at current rates, exclusive of the proposed RES
 Tariff in Docket No. E-01575A-07-0310.

28 ⁴ The Staff Report does not estimate the revenues expected to be collected from the proposed RES Tariff.

1 recognizes that the inclusion of the \$75.46 million in new debt for the 2008-2009 CWP in
2 conjunction with the requested \$11.48 million in the current application results in an overly leveraged
3 financial position. Staff states, however that there is no other known immediate option to finance the
4 CWP. Staff also notes that in the long-run, increased rates would provide additional equity.
5 Furthermore, the Cooperative expects the RES Tariff to cover repayment of the CREBS Program
6 debt.

7 18. Staff states that SSVEC has no compliance issues.

8 19. Staff concludes that issuance of the proposed debt financing for the purposes stated in
9 the application is within SSVEC's corporate powers, is compatible with the public interest, is
10 consistent with sound financial practices and will not impair SSVEC's ability to provide service.

11 20. Staff recommends that the Commission authorize SSVEC's request to obtain CREBS
12 Program financing through a credit facility not to exceed \$11.48 million from CFC and to pledge,
13 mortgage, lien and/or encumber its assets; that SSVEC be authorized to engage in any transaction and
14 to execute any documents necessary to effectuate the authorizations granted; and that SSVEC file one
15 copy of the executed loan documents with Docket Control within 60 days of execution.

16 21. We find that Staff's recommendations are reasonable and should be adopted,
17 however, our approval is conditioned on the approval of a RES Tariff that would provide funds for
18 repayment of the loan. At our November 27, 2007, Open Meeting we authorized SSVEC to borrow
19 \$70.78 million from the CFC for its 2008-2009 CWP, and we directed SSVEC to file a report of its
20 equity projections if it has not filed a rate case before December 31, 2009, and its equity is less than
21 23 percent of its total capital. That requirement remains in effect and will allow the Commission to
22 monitor the effect of both loan facilities on the Cooperative's capital structure.

23 CONCLUSIONS OF LAW

24 1. SSVEC is a public service corporation within the meaning of Article XV of the
25 Arizona Constitution and A.R.S. §§ 40-301, 40-302, and 40-303 and AAC R14-2-1814.

26 2. The Commission has jurisdiction over SSVEC and of the subject matter of the
27 application.

28 3. Notice of the application was given in accordance with the law.

1 4. The financing approved is for lawful purposes within SSVEC's corporate powers, is
2 compatible with the public interest, with sound financial practices, and with the proper performance
3 by SSVEC of service as a public service corporation, and will not impair its ability to perform the
4 service.

5 5. The financing approved herein is for the purposes stated in the application, is
6 reasonably necessary for those purposes, and such purposes are not, wholly or in part, reasonably
7 chargeable to operating expenses or to income.

8 **ORDER**

9 IT IS THEREFORE ORDERED that Sulphur Springs Valley Electric Cooperative, Inc. is
10 hereby authorized to borrow up to \$11,480,000 of long term debt from the National Rural Utilities
11 Cooperative Finance Corporation at an interest rate not to exceed 0.5 percent, for the purposes set
12 forth in the application and set forth herein, conditioned on the approval of a compatible RES Plan
13 and Tariff that include the CREBS Program.

14 IT IS FURTHER ORDERED that Sulphur Springs Valley Electric Cooperative, Inc. is
15 authorized to pledge, mortgage, lien and/or encumber its assets in connection with the loan approved
16 herein.

17 IT IS FURTHER ORDERED that Sulphur Springs Valley Electric Cooperative, Inc. is
18 authorized to engage in any transactions and to execute or cause to be executed any documents or
19 modifications to existing documents to effectuate the authorization granted herein, including notes
20 and bonds evidencing or securing the indebtedness authorized herein.

21 IT IS FURTHER ORDERED that such finance authority shall be expressly contingent upon
22 Sulphur Springs Valley Electric Cooperative, Inc.'s use of the proceeds for the purposes stated in the
23 application and approved herein.

24 IT IS FURTHER ORDERED that Sulphur Springs Valley Electric Cooperative, Inc. shall file
25 with Docket Control, as a compliance item in this docket, its executed financing documents within 60
26 days after the date of execution.

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28 ...

1 IT IS FURTHER ORDERED that approval of the financing set forth hereinabove does not
2 constitute or imply approval or disapproval by the Commission of any particular expenditure of the
3 proceeds derived thereby for purposes of establishing just and reasonable rates.

4 IT IS FURTHER ORDERED that this Decision shall become effective immediately.

5 BY ORDER OF THE ARIZONA CORPORATION COMMISSION.
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8 CHAIRMAN

COMMISSIONER

10 COMMISSIONER

COMMISSIONER

COMMISSIONER

13 IN WITNESS WHEREOF, I, DEAN S. MILLER, Interim
14 Executive Director of the Arizona Corporation Commission,
15 have hereunto set my hand and caused the official seal of the
16 Commission to be affixed at the Capitol, in the City of Phoenix,
17 this ____ day of _____, 2007.

18 DEAN S. MILLER
19 INTERIM EXECUTIVE DIRECTOR

22 DISSENT _____

24 DISSENT _____

JR:db

1 SERVICE LIST FOR: SULPHUR SPRINGS VALLEY ELECTRIC COOPERATIVE, INC.

2 DOCKET NO.: E-01575A-07-0501

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